



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

**REPORT OF THE AUDITOR – GENERAL TO THE NORTHERN CAPE
PROVINCIAL LEGISLATURE AND THE COUNCIL ON THE FINANCIAL
STATEMENTS AND PERFORMANCE INFORMATION OF HANTAM
MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2009**

**REPORT OF THE AUDITOR-GENERAL TO THE NORTHERN CAPE PROVINCIAL
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ENDED 30 JUNE 2009**

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the accompanying financial statements of the Hantam Municipality which comprise the statement of financial position as at 30 June 2009, and the statement of financial performance, the statement of changes in net assets and the cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages [xx] to [xx].

The accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the effective Statements of General Recognised Accounting Practice (GRAP), including any interpretations and directives issued by the Accounting Standards Board (ASB), as set out in accounting policy note 1 and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA) and for such internal control as the accounting officer determines is necessary, to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Auditor-General's responsibility

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with the International Standards on Auditing read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008*. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. Paragraph 11 *et seq.* of the Statement of Generally Recognised Accounting Practice, GRAP 1 *Presentation of Financial Statements* requires that financial reporting by entities shall provide information on whether resources were obtained

and used in accordance with the legally adopted budget. As the budget reporting standard is not effective for this financial year, I have determined that my audit of any disclosures made by the Hantam Municipality in this respect will be limited to reporting on non-compliance with this disclosure requirement.

7. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my audit opinion.

Basis for qualified opinion

Property, plant and equipment

8. The completeness and valuation of property, plant and equipment amounting to R66 530 950, disclosed in note 6 to the financial statements, could not be confirmed. I was unable to satisfy myself by alternative means concerning the following inconsistencies and scope limitations:

- Differences between depreciation amounts recalculated and the amounts as per the asset register amounted to R2 865 749. No explanation could be obtained for this difference.
- Differences between accumulated depreciation amounts recalculated and the amounts as per the asset register amounted to R4 250 655. No explanation could be obtained for this difference.
- Assets to the amount of R460 132 (2008: R56 400) appearing on the valuation roll could not be traced to the asset register and were therefore not included on the financial statements.
- The completeness of the asset register could not be confirmed as several assets were selected from their physical locations, but could not be traced to the asset register. Owing to this limitation in the detail contained in the asset register, no alternative procedures could be performed.
- An error in the asset register was corrected in the asset register, but not in the financial statements. This brought about an overstatement of property, plant and equipment and the revaluation reserve of R252 269.
- The correction of a prior year error amounting to R12 019 694 as disclosed in the statement of changes in net assets, included a difference amounting to R11 506 299 between the revaluation amount of property, plant and equipment as per note 6 to the annual financial statements and the movement in the revaluation reserve. I could not obtain sufficient appropriate audit evidence for the unexplained difference amounting to R11 506 299.

Debtors

9. I was unable verify the completeness, rights, existence and valuation of debtors amounting to R17 781 068, as disclosed in note 8 to the financial statements because the municipality made a blanket provision of R7 350 053 for impairment of debtors. The South African Statement of Generally Accepted Accounting Practice, IAS 39 (paragraphs 63 and 64), *Financial Instruments* does not allow blanket impairment provisions. In terms of IAS 39 the municipality must assess at each reporting date whether a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is deemed to be impaired if, and only if, there is objective evidence of impairment. I could not obtain evidence for the basis

of impairment of R7 350 053. The records of the municipality did not permit the application of alternative audit procedures.

Revenue

10. The unspent balance at the beginning of the year of unspent conditional grants was not taken into account in the transfer of unspent conditional grants for which the conditions of the grant have been met, to revenue. The effect of this is that revenue is understated and unspent conditional grants overstated by the aforementioned amount.
11. The municipality incorrectly allocated divisional expenses to the rental income account. Expenditure and rental income were thus overstated by R1 592 456.
12. Payables are misstated in the financial statements, as unallocated deposits amounting to R110 687 are included in payables. This effect on revenue and debtors for the said amount could not be determined.

Employee benefits

13. I was unable to verify the completeness, obligations, existence, valuation and classification of employee benefit obligations, due to the following:
 - The municipality provides for post-retirement medical benefits by subsidising certain retired staff according to the rules of the medical aid funds. The municipality did not accrue for the expected costs of these benefits in accordance with the South African Statement of Generally Accepted Accounting Practice, IAS 19, *Employee Benefits*. In terms of IAS 19, all post-employment benefit plans are defined as defined benefit plans and these plans may be funded, partially funded or unfunded. The municipality must account for the obligation using the projected credit unit method to measure its obligations and costs. In the absence of an actuarial valuation, I could not confirm the obligations, current service costs, interest costs and accumulated actuarial gains/losses.
 - No disclosure was made of long-term service bonuses, as required by IAS 19. I was unable to determine the understatement of the obligation, due to the lack of sufficient appropriate audit evidence.

Qualified opinion

14. In my opinion, except for the possible effects of the matters described in the basis for qualified opinion paragraphs, the financial statements present fairly, in all material respects, the financial position of the Hantam Municipality as at 30 June 2009 and its financial performance and its cash flows for the year then ended, in accordance with the basis of accounting set out in accounting policy note 1, and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMA).

Other matters

I draw attention to the following matters that relate to my responsibilities in the audit of the financial statements:

Unaudited supplementary schedules

15. The municipality provided supplementary information in the financial statements on whether resources were obtained and used in accordance with its legally adopted budget, in accordance with GRAP 1, *Presentation of Financial Statements*. The supplementary budget information set out on pages XX to XX does not form part of the financial statements and is provided as additional information.

Non-compliance with applicable legislation

Municipal Finance Management Act

16. The mayor did not approve the municipality's service delivery and budget implementation plan within 28 days after the approval of the budget as required by section 53(c)(ii) of the MFMA.
17. The municipality did not implement the approved service delivery budget implementation plan and therefore reasonable steps have not been taken to ensure that the spending of funds is in accordance with the budget and is reduced as necessary when revenue is anticipated to be less than projected in the budget or in the service delivery and budget implementation plan. This is in contravention of section 69(1)(1) of the MFMA.
18. The annual report was made public and the local community was invited to submit representation in connection with the annual report one month after the annual report was tabled and not immediately as required by section 127(5) of the MFMA.
19. A draft service delivery and budget implementation plan was not submitted to the mayor within 14 days after approval of the annual budget as required by section 69(3) of the MFMA.
20. The accounting officer did not within 30 days after the end of each quarter table in the municipal council a consolidated report of all withdrawals from bank accounts made in terms of subsection (1)(b) to (j) of section 11(4) of the MFMA.

Supply chain management

21. Supply chain management officials did not declare their interest in contracts by signing any declaration forms. This resulted in a declaration register not being kept and maintained, which is in contravention of regulation 46 of the Supply Chain Management Regulations.

Governance framework

22. The governance principles that impact the auditor's opinion on the financial statements are related to the responsibilities and practices exercised by the accounting officer and executive management and are reflected in the internal control deficiencies and key governance requirements addressed below:

Internal control deficiencies

23. Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of

financial and risk management and internal control. The table below depicts the root causes that gave rise to the deficiencies in the system of internal control, which led to the qualified opinion. The root causes are categorised according to the five components of an effective system of internal control. In some instances deficiencies exist in more than one internal control component.

Par. no.	Basis for qualified opinion	CE	RA	CA	IC	M
8	Property, plant and equipment	1,5		1,3,4,5		2
9	Debtors	1,2,5		1,2,5		
10 - 12	Revenue	5,6,7	1	3,5	1	
13	Employee benefits	1,2,5,6	1,2	1,3,5		2

Legend	
CE = Control environment	
The organisational structure does not address areas of responsibility and lines of reporting to support effective control over financial reporting.	1
Management and staff are not assigned appropriate levels of authority and responsibility to facilitate control over financial reporting.	2
Human resource policies do not facilitate effective recruitment and training, disciplining and supervision of personnel.	3
Integrity and ethical values have not been developed and are not understood to set the standard for financial reporting.	4
The accounting officer/accounting authority does not exercise oversight responsibility over financial reporting and internal control.	5
Management's philosophy and operating style do not promote effective control over financial reporting.	6
The entity does not have individuals competent in financial reporting and related matters.	7
RA = Risk assessment	
Management has not specified financial reporting objectives to enable the identification of risks to reliable financial reporting.	1
The entity does not identify risks to the achievement of financial reporting objectives.	2
The entity does not analyse the likelihood and impact of the risks identified.	3
The entity does not determine a risk strategy/action plan to manage identified risks.	4
The potential for material misstatement due to fraud is not considered.	5
CA = Control activities	
There is inadequate segregation of duties to prevent fraudulent data and asset misappropriation.	1
General information technology controls have not been designed to maintain the integrity of the information system and the security of the data.	2
Manual or automated controls are not designed to ensure that the transactions have occurred, are authorised, and are completely and accurately processed.	3
Actions are not taken to address risks to the achievement of financial reporting objectives.	4
Control activities are not selected and developed to mitigate risks over financial reporting.	5
Policies and procedures related to financial reporting are not established and	6

communicated.	
Realistic targets are not set for financial performance measures, which are in turn not linked to an effective reward system.	7
IC = Information and communication	
Pertinent information is not identified and captured in a form and time frame to support financial reporting.	1
Information required to implement internal control is not available to personnel to enable internal control responsibilities.	2
Communications do not enable and support the understanding and execution of internal control processes and responsibilities by personnel.	3
M = Monitoring	
Ongoing monitoring and supervision are not undertaken to enable an assessment of the effectiveness of internal control over financial reporting.	1
Neither reviews by internal audit or the audit committee nor self -assessments are evident.	2
Internal control deficiencies are not identified and communicated in a timely manner to allow for corrective action to be taken.	3

Key governance responsibilities

24. The MFMA tasks the accounting officer with a number of responsibilities concerning financial and risk management and internal control. Fundamental to achieving this is the implementation of key governance responsibilities, which I have assessed as follows:

No.	Matter	Y	N
Clear trail of supporting documentation that is easily available and provided in a timely manner			
1.	No significant difficulties were experienced during the audit concerning delays or the availability of requested information.	x	
Quality of financial statements and related management information			
2.	The financial statements were not subject to any material amendments resulting from the audit.		x
3.	The annual report was submitted for consideration prior to the tabling of the auditor's report.		x
Timeliness of financial statements and management information			
4.	The annual financial statements were submitted for auditing as per the legislated deadlines in section 126 of the MFMA.	x	
Availability of key officials during audit			
5.	Key officials were available throughout the audit process.	x	
Development and compliance with risk management, effective internal control and governance practices			

No.	Matter	Y	N
6.	Audit committee		
	<ul style="list-style-type: none"> The municipality had an audit committee in operation throughout the financial year. 		x
	<ul style="list-style-type: none"> The audit committee operates in accordance with approved, written terms of reference. 		x
	<ul style="list-style-type: none"> The audit committee substantially fulfilled its responsibilities for the year, as set out in section 166(2) of the MFMA. 		x
7.	Internal audit		
	<ul style="list-style-type: none"> The municipality had an internal audit function in operation throughout the financial year. 		x
	<ul style="list-style-type: none"> The internal audit function operates in terms of an approved internal audit plan. 		x
	<ul style="list-style-type: none"> The internal audit function substantially fulfilled its responsibilities for the year, as set out in section 165(2) of the MFMA. 		x
8.	There are no significant deficiencies in the design and implementation of internal control in respect of financial and risk management.		x
9.	There are no significant deficiencies in the design and implementation of internal control in respect of compliance with applicable laws and regulations.	x	
10.	The information systems were appropriate to facilitate the preparation of the financial statements.	x	
11.	A risk assessment was conducted on a regular basis and a risk management strategy, which includes a fraud prevention plan, is documented and used as set out in section 62(1)(c)(i) of the MFMA.		x
12.	Delegations of responsibility are in place, as set out in section 79 of the MFMA.	x	
Follow-up of audit findings			
13.	The prior year audit findings have been substantially addressed.		x
14.	SCOPA/Oversight resolutions have been substantially implemented.	n/a	
Issues relating to the reporting of performance information			
15.	The information systems were appropriate to facilitate the preparation of a performance report that is accurate and complete.		x
16.	Adequate control processes and procedures are designed and implemented to ensure the accuracy and completeness of reported performance information.		x
17.	A strategic plan was prepared and approved for the financial year under review for purposes of monitoring the performance in relation to the budget and delivery by the municipality against its mandate, predetermined objectives, outputs, indicators and targets section 68 of the MFMA.		x
18.	There is a functioning performance management system and performance		x

No.	Matter	Y	N
	bonuses are only paid after proper assessment and approval by those charged with governance.		

Clear trail of supporting documentation

25. The accounting officer is responsible for keeping proper records of the financial affairs of the municipality. Leadership should monitor transactions and events on an ongoing basis to ensure proper recognition and disclosure in the financial statements and that adequate supporting documentation exists and is properly filed.

The financial statements compiled were not supported by proper and complete sufficient appropriate supporting documentation to facilitate the audit process. The accounting officer should ensure that a proper review is performed on the financial statements and that supporting documentation and an accounting file exists to support the financial statements.

Quality of financial statements

26. Material amendments were made to the financial statements relating to property, plant and equipment, employee benefits, creditors, debtors, statement of changes in net assets, disclosures and notes to the financial statements. The material amendments were identified by the auditors during the audit and not the internal controls of the municipality or the consultants who prepared the financial statements. There should be a discipline to produce monthly financial statements and management information for review by management.

Risk management, internal control and governance

27. The municipality did not have an audit committee or an internal audit function during the year. Management should liaise with their district municipality to assist with these functions as shared functions are allowed by the MFMA. Internal audit and audit committee functions are imperative to ensure the proper implementation and monitoring of internal control.

Inadequate accounting and internal control policies existed at the municipality, resulting in various cases of non-compliance with legislation and accounting guidelines.

Management should develop and implement an adequate fraud prevention plan. This needs to be communicated to all staff within the municipality to ensure adherence thereof.

The implementation of audit recommendations requires improved monitoring and supervision by management.

Reporting of performance information

28. There is no performance information system in place at the municipality. The IDP is also inadequate as it does not have key performance indicators. The IDP and budget also are not aligned. Detailed standard operating procedures setting out the roles and responsibilities of all levels of staff involved in the collection and collation of performance information, from source document to reporting, has not been

prepared and communicated throughout the entire municipality. This is indicative of a situation where adequate control processes and procedures were not designed and implemented to ensure the accuracy and completeness of reported performance information and adequate mechanisms were not established to monitor and review the performance management system.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

Report on performance information

29. I was engaged to review the performance information.

The accounting officer's responsibility for the performance information

30. In terms of section 121(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality, prepared by the municipality in terms of section 46 of the Local Government: Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA).

The Auditor-General's responsibility

31. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 616 of 2008*, issued in *Government Gazette No. 31057 of 15 May 2008* and section 45 of the MSA.
32. In terms of the foregoing my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.
33. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the findings reported below.

Findings on performance information

No reporting on performance information

34. The annual report of the municipality did not include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA, as required by section 121(3)(c) of the MFMA. As a consequence the consistence and reliability of performance information could not be tested and verified.

Content of integrated development plan

35. Key performance indicators were not set as described in the act as no differentiation was made between input indicators, output indicators and outcome indicators. The performance, management system structure was there, but has not yet been implemented as at 30 June 2009. This constitutes non-compliance with Regulation 9 of the Local Government: Municipal Planning and Performance Management Regulations (2001).
36. The municipality did not set performance targets for each of its key performance indicators as required by Regulation 12 of the Local Government: Municipal Planning and Performance Management Regulations (2001).

Implementation of the performance management system

37. The municipality has a developed performance management system, which has not been implemented and which brought about that no reporting was done on performance information. This is in contravention of section 46(1) of the Municipal Systems Act.
38. No process or mechanism has been established to evaluate the staff establishment.
The performance of staff is not monitored, measured or evaluated.
The above is in contravention of section 66 of the Municipal Systems Act.
39. The IDP does not reflect the council's development priorities and objectives for its elected term as well as any key performance indicators and performance targets as is required by section 26 of the Municipal Systems Act.
40. Notice was not given within 14 days of the adoption of the municipality's integrated development plan to the public of its adoption of its integrated development plan, which is in contravention of section 25(4) of the Municipal Systems Act.
41. A copy of the integrated development plan as adopted by the council of the municipality was submitted, but not within 10 days of adoption to the MEC for Local Government in the province as required by section 32(1)(a) of the Municipal Systems Act.
42. The municipality does not have a PMS framework in place. Although the framework is available, it is not yet implemented as required by section 41 of the Municipal Systems Act.
43. The mayor of the municipality did not manage the development of the PMS required by section 39 of the Municipal Systems Act.

Existence and functioning of a performance audit committee

44. The Hantam Municipality did not appoint and budget for a performance audit committee, nor was another audit committee utilised as the performance audit committee, as required by regulation 14(2) of the of the Municipal Planning and Performance Management Regulations, 2001.

No mid-year budget and performance assessments

The accounting officer of the Hantam Municipality did not assess the performance of the municipality during the first half of the financial year, taking into account the municipality's services delivery performance during the first half of the financial year and the service delivery and performance indicators set in the service delivery and budget implementation plan, as required by section 72 of the MFMA.

APPRECIATION

45. The assistance rendered by the staff of the Hantam Municipality during the audit is sincerely appreciated.

Auditor - General.

Kimberley

1 December 2009



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